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In the

Supreme Court of the United States

OCTOBER TERM, 1990

TOWN OF CONCORD, MASSACHUSETTS and
TOWN OF WELLESLEY, MASSACHUSETTS,
Petitioners,

v.

BOSTON EDISON COMPANY,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIRST CIRCUIT

BRIEF FOR THE CITIES OF ANAHEIM, RIVERSIDE, BANNING, COLTON AND AZUSA, CALIFORNIA AS AMICI CURIAE IN SUPPORT OF THE PETITIONERS

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February 22, 1991

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INTEREST OF THE AMICI CURIAE

Counsel for both petitioners and respondent have consented to the filing of this brief. The consents are being filed with this Court.

The Cities of Anaheim, Riverside, Banning, Colton, and Azusa, California ("Cities") own and operate municipal electric utility systems. Historically, each has been dependent upon Southern California Edison Company ("SCE") for all or substantially all of its bulk power requirements. While that dependency has lessened in recent years, considerable uncertainty exists as to the future, and there is a real possibility that the Cities may again become largely dependent upon SCE for bulk power.

Each of the Cities is surrounded by territory which SCE serves at retail, and each competes with SCE in the ways described by the United States Court of Appeals for the Second Circuit in *City of Groton v. Connecticut Light & Power Co.*, 662 F.2d 921, 934 (2d Cir. 1981). During the period 1976-1979, the Cities were victimized by a "price squeeze" imposed on them by SCE, which charged the Cities higher prices at wholesale than it charged its own retail customers for comparable service. The Cities have received partial relief for the price squeeze from the Federal Energy Regulatory Commission ("FERC"),[1] but have been denied relief by the United States District Court for the Central District of California.[2] Both SCE and the Cities have filed petitions for review of the FERC's price squeeze decision with the United States Court of Appeals for the District of Columbia Circuit.[3] An appeal is pending in the United States Court of the Appeals for the Ninth Circuit from the adverse decision of the district court.[4] As victims of a price squeeze and as litigants seeking antitrust protection from such conduct, each of the Cities has a vital interest in the outcome of this litigation and resolution of the present conflict in the law.

The decision of the First Circuit in *Town of Concord v. Boston Edison Co.*, 915 F.2d 17 (1st Cir. 1990)("Concord"), *petition for*

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[1] *Southern California Edison Co.*, Opinion No. 284, 40 F.E.R.C. ¶ 61,371 (1987), *on rehearing*, Opinion No. 284-A, 50 F.E.R.C. ¶ 61,275 (1990), *appeals docketed*, No. 90-1236 (D.C. Cir. May 4, 1990), No. 90-1369 (D.C. Cir. July 16, 1990).

[2] *Cities of Anaheim, et al. v. Southern California Edison Co.*, 1990-2 Trade Cases (CCH) ¶ 69,246 (C.D. Cal. 1990), *appeal docketed*, No. 90-56375 (9th Cir. Nov. 15, 1990).

[3] Nos. 90-1236 and 90-1369 in the United States Court of Appeals for the District of Columbia Circuit.

[4] No. 90-56375 in the United States Court of Appeals for the Ninth Circuit.

cert. filed, 59 U.S.L.W. 3526 (U.S. Jan. 22, 1991)(No. 90-1168), effectively denies access to federal courts for antitrust claims that are significant to consumer welfare and that implicate congressional policy, this Court's decisions, and sound public policy. Moreover, the *Concord* decision is in direct conflict with decisions of at least three other circuits. Given the nature of the regulatory environment in which the Cities and SCE function, it is crucial that the First Circuit decision be reversed so that prospective litigants will not be deprived of a forum in which to litigate their claims of abuse of monopoly power.

SUMMARY OF ARGUMENT

Notwithstanding this Court's square holdings that neither federal nor state regulation of an electric utility operates to implicitly repeal the application of the antitrust laws, *see Otter Tail Power Co. v. United States,* 410 U.S. 366 (1973), *and Cantor v. Detroit Edison Co.,* 428 U.S. 579 (1976), the First Circuit has fashioned an inflexible rule tantamount to repeal in one of the most active areas of antitrust-regulatory interplay, the price squeeze imposed on a customer-competitor of a wholesale/retail monopolist. This remarkable result is achieved by economic theorizing which predicts that in a regulated context, a price squeeze simply cannot constitute exclusionary behavior violative of Section 2 of the Sherman Act, 15 U.S.C. § 2. If so, three circuit court decisions (and several district court rulings) recognizing and applying the opposite legal proposition, that a price squeeze in the regulated electric utility industry can be an invidious anticompetitive practice requiring antitrust scrutiny, are wrong: *City of Mishawaka v. American Electric Power Co.,* 616 F.2d 976 (7th Cir. 1980) ("*Mishawaka II*"), *cert. denied,* 449 U.S. 1096 (1981); *City of Groton v. Connecticut Light & Power Co.,* 662 F.2d 921 (2d Cir. 1981); *City of Kirkwood v. Union Electric Co.,* 671 F.2d 1173 (8th Cir. 1982), *cert. denied,* 459 U.S. 1170 (1983).

The bedrock deficiency of the opinion below is that it believes that competition can or should play no consumer welfare role in the regulated industries. It prefers to dispense with the market in favor of total regulation. In doing so, it flatly contradicts congressional policy, numerous decisions of this Court, and practical wisdom.

The opinion below also relies on regulatory difficulties which might be created by simultaneous antitrust and administrative remedies to justify limitation of access to federal courts. The argument is not sound. Direct regulation of prices by federal and state agencies is not degraded by the imperatives of the competitive process. In fact, competition, which promotes consumer welfare, actually facilitates more effective regulation. Accordingly, the resolution of any actual conflict between antitrust policy and regulation should be left to a case-by-case determination, not an inflexible economic model.

Finally, in arguing that the FERC can solve these problems, the First Circuit misunderstands the process. The FERC cannot restore the affected municipal utility to the status quo. Under present law, a proposed wholesale rate is effective when accepted for filing. During the pendency of the price squeeze, competition is suppressed or eliminated. Without the deterrent of treble damages, costs, attorneys' fees and possible injunctive relief, there is no incentive for the monopolist to refrain from exploiting its smaller competitors and suppressing their competitive capability and zeal. It is the threat of treble damage litigation and only that threat which will deter anticompetitive price squeeze conduct.

In the guise of economic analysis, the First Circuit has created a discordant and extraordinarily dangerous precedent. We urge this Court to grant certiorari and reverse.

ARGUMENT

I.

THE PREDICATE OF THE CONCORD DECISION—THAT A PRICE SQUEEZE PRODUCES NO ANTICOMPETITIVE HARM OR CONSUMER INJURY—IS INCONSISTENT WITH FUNDAMENTAL NATIONAL POLICY AS WELL AS DECISIONS OF THIS COURT AND THREE OTHER CIRCUITS

Despite its frequent disclaimers, *Concord* amounts to a repudiation of the antitrust laws in regulated industry pricing cases. Such a result could not be achieved directly. *See Otter Tail,* 410

U.S. 366; *Cantor*, 428 U.S. 579. There is no jurisprudential basis to allow that result to be achieved indirectly by a predetermination, based on unsubstantiated and fallacious economic theory, that certain conduct simply cannot produce an anticompetitive result. Not only has this Court rejected implied repeal in the electric utility industry (whether regulated by federal or state agencies), lower courts have consistently refused to apply either the doctrine of exclusive jurisdiction, *see City of Mishawaka v. Indiana & Michigan Electric Co.*, 560 F.2d 1314, 1318-21 (7th Cir. 1977)("*Mishawaka I*"), *cert. denied*, 436 U.S. 922 (1978), or the so-called "filed rate" doctrine to price squeeze cases, *see Kirkwood*, 671 F.2d at 1177-79. Yet, the import of *Concord* is to override all these prior reasoned decisions and repeal antitrust as a remedy in favor of regulatory exclusivity. That result should not be accepted.

This Court has held decisively and consistently that antitrust policy is applicable to the electric utility industry, that regulation is not inherently incompatible with competition, and that the FERC and the courts have joint responsibility for effectuating antitrust policy in that industry.

California v. FPC, 369 U.S. 482, 490 (1962), made clear that the courts retain the responsibility for enforcing the antitrust laws. In holding that FPC (now FERC) review of a proposed merger should await the outcome of a pending antitrust action in district court, the Court expressed concern that "antitrust policy whose enforcement Congress in this situation has entrusted to the courts" would "in practical effect [be] taken over by the Federal Power Commission." Later, in *Gulf States Utilities Co. v. FPC*, 411 U.S. 747, 760 (1973), this Court envisioned a relationship between the FPC and the antitrust laws in which "[c]onsideration of antitrust and anticompetitive issues by the Commission . . . serves the important function of establishing a first line of defense against those competitive practices that might later be the subject of antitrust proceedings." This Court, therefore, has held plainly at least twice that jurisdiction to resolve antitrust claims arising out of utility conflicts remains with the courts, not the FERC. The First Circuit's decision flatly disregards these teachings.

Moreover, if the *Concord* court's determination that price squeeze almost never results in an anticompetitive effect is valid, then the decision of this Court in *FPC v. Conway Corp.*, 426 U.S. 271 (1976), is meaningless. In *Conway*, this Court directed the FPC to consider the anticompetitive effects of an alleged price squeeze in determining whether, and to what extent, it should approve a proposed wholesale rate increase. The Court ruled that the FPC had to arrive at a rate which was "just and reasonable" and "in doing so it *must* consider the tendered allegations that the proposed rates are discriminatory and anticompetitive in effect." *Id.* at 279 (emphasis added). It is true that this Court, in dealing with what may be characterized as a pleading issue, did not find or even suggest in *Conway* that there were actual anticompetitive effects. But one must assume this Court would not have mandated a futile undertaking. Accordingly, *Conway* must be read as acknowledging the distinct possibility that a price squeeze could have an anticompetitive effect. Read as a guidepost for *Mishawaka II*, 616 F.2d 976, which on a full trial record found actual anticompetitive effects, it is difficult to conceive that the academic exercise of the First Circuit was more than an attempt to deny the obvious: Price squeezes do exist and they can and do pinch.

The irreconcilable conflicts between the *Concord* decision and the *Mishawaka II*, *Kirkwood*, and *Groton* decisions of the Seventh, Eighth, and Second Circuits have been described in detail in the January 22, 1991 Petition for a Writ of Certiorari filed by the Towns of Concord and Wellesley, Massachusetts ("Towns"). The Cities will not repeat that discussion but instead will supplement the Towns' Petition by identifying fundamental flaws in the economic analysis relied upon in the *Concord* decision and, in so doing, demonstrate its inconsistency not only with the decisions of other circuits and of this Court but also with the fundamental principles underlying the antitrust laws.

The positive effects of competition in the electric utility industry have been summarized eloquently by Alfred Kahn:

> We do not consider here whether public enterprise is superior or inferior to private enterprise as an instrument for getting the world's work done . . . . But there is strong evidence in the

> public utility arena that *competition between* the two systems of organization, like competition among private businesses, is highly conducive to improved performance. It may take the form of direct rivalry (for the patronage of the same customers in the same market); or of competition-by-example (where comparisons may be drawn between the performances of private and public enterprises in serving their respective customers, in different markets); or by threat of total displacement (where the management of each is aware that voters are examining its performance with the possibility of substituting one system of control for the other). . . .
>
> The most familiar illustration of this kind of competition in the United States has been in the field of electric power. . . .
>
> . . . The fact is that the competition-by-example or by threat of displacement by public enterprise has greatly improved the performance of this industry. The competition of public with private power has probably been a much more powerful influence than regulation in this respect, and particularly in bringing about dynamic price reduction, sales promotion, and extension of service.

2 A. Kahn, *The Economics of Regulation,* 104-06 (1971)(Footnotes omitted). *See also* Meeks, *Concentration in the Electric Power Industry: The Impact of Antitrust Policy,* 72 Colum. L. Rev. 64 (1972)(cited with approval in *Gulf States,* 411 U.S. at 758, 759; *Groton,* 662 F.2d at 929, 930, 934; and *Conway Corp. v. FPC,* 510 F.2d 1264, 1268 (D.C. Cir. 1975), *aff'd,* 426 U.S. 271 (1976)). The economic theory propounded by the *Concord* decision, however, ultimately rests upon disdain for the value of competition in the regulated electric utility industry. An evaluation of examples from the analysis set forth in the *Concord* opinion makes clear that its conclusions are premised upon a profound distrust or disregard for the competitive process. This premise is totally wrong.

The *Concord* court's unwillingness to accept the importance of competition permeates the opinion. First, the decision opines that a "primary-level monopolist might carry out its second-level activities more efficiently than its independent competitors," in which case the elimination of the second-level competitors would

be economically desirable. *Concord* at 15a. [5] The short answer to this example is that permitting the primary-level monopolist to engage in price squeeze is totally unnecessary to achieve the desired result and is equally likely to lead to undesired consequences. If the primary-level monopolist is truly more efficient in the performance of the second-level activities, it should be able to eliminate the less efficient second-level competitors by vigorous competition alone. Moreover, allowing the primary-level monopolist to indulge in price squeeze is at least equally likely to lead to the suppression or elimination of competitors who are *more* efficient in the performance of the second-level activities. The *Concord* court's rationale would allow the primary-level monopolist the unfettered ability to control the existence and vigor of competition at the second level, rather than properly relying on the competitive process to weed out inefficient players. [6]

The *Concord* opinion also suggests that a price squeeze could be economically beneficial if the second-level firm subjected to the squeeze is itself a monopolist. *Concord* at 15a-16a. This paradigm, however, is simply not applicable in the vast majority of cases involving price squeeze in the electric utility industry. Although retail distribution of electricity exhibits natural monopoly characteristics, municipal systems such as the Cities and Towns typi-

[5] Citations to the *Concord* opinion are to the copy of the decision appended to the Towns' January 22, 1991 Petition for a Writ of Certiorari.

[6] In part, the *Concord* court's sanguine attitude can be traced to the notion that the antitrust laws should be indifferent to a monopolist's exploitation of monopoly power because extant power is a fixed sum and thus will result in the same damage regardless of how it is deployed. This theory has been roundly criticized by economists. *See* Kaplow, *Extension of Monopoly Power Through Leverage*, 85 Colum. L. Rev. 515 (1985). As Kaplow observes, the "fixed sum" perception of power is strongly counterintuitive. His analogy of a monopolist with power to a terrorist on the loose with one stick of dynamite shows the folly of presuming that the law is indifferent to where the power (or dynamite) is placed. *Id.* at 516. Moreover, even some who initially proposed the model have recognized that it may not apply in the context of regulated industries. *Olympia Equipment Leasing Co. v. Western Union Telegraph Co.*, 797 F.2d 370, 374 (7th Cir. 1986), *cert. denied*, 480 U.S. 934 (1987).

cally are surrounded by the service area of the seller utility that is imposing the price squeeze, and their retail rates are constrained by the rates of the surrounding system. *Conway Corp. v. FPC,* 510 F.2d at 1268-69.

Having posited the foregoing fallacious reasons why price squeeze might be a good thing in general, the *Concord* opinion goes on to offer five reasons why the antitrust courts should not be concerned about a price squeeze in the context of a regulated industry. Those reasons are equally invalid and equally inconsistent with the fundamental concern for the competitive process that is the bedrock of antitrust policy.

The *Concord* decision first asserts that in a regulated industry, price squeeze is unlikely to have adverse effects because the regulators directly control prices as well as market entry and exit. *Concord* at 18a-19a. These arguments rest on the discredited assumption that competition has no role in the electric utility industry and are irreconcilable with this Court's rulings in *Conway,* 426 U.S. 271, and *Otter Tail,* 410 U.S. 366. Contrary to the circuit court's apparent assumption, price regulation is not a perfect science, as this Court expressly recognized in *Conway,* 426 U.S. at 278-79. Moreover, the circuit court's rationale ignores the fact that competition can induce improvements in productive efficiency, resulting in lower costs and, indirectly, lower prices. [7] The *Otter Tail* case also refutes the suggestion that regulators can prevent a monopolist utility from creating barriers to entry. In that case, the Court found that Otter Tail had done exactly what *Concord* claims regulation would prevent a utility from doing, *i.e.,* creating barriers to entry by refusals to deal and other means.

The *Concord* court's observation that regulators must approve a take-over of a municipal system also reflects a fundamental misunderstanding or disregard of the competitive process. The circuit court apparently assumes that so long as competitors are permitted to survive, a price squeeze works no harm on the competitive process. But, just as the elimination of competitors does not necessarily signify harm to the competitive process, *cf. Bruns-*

[7] Even when regulation succeeds in setting prices equal to costs, it has difficulty in determining whether costs are as low as feasible.

wick Corp. v. Pueblo Bowl-O-Mat Inc., 429 U.S. 477 (1977), the continued survival of competitors does not negate injury to competition. If a price squeeze prevents competitors from competing as vigorously as they could have in the absence of price squeeze, the competitive process is harmed, even if the competitors manage to survive.

In addition to its supply relationship with each of the Cities, SCE serves at retail the territory surrounding these municipal systems. SCE competes with the Cities in the retail market despite the regulation of its retail electricity prices by the California Public Utilities Commission and oversight of interstate power transactions by the FERC. Not only is there franchise competition between these entities for who will secure and retain a franchise to serve particular areas, but yardstick competition also exists by virtue of a regulatory and political process that compares each utility's performance against the others'. The efficiencies of compared systems provide regulators with insights regarding the appropriate level for each monopolist's rates and returns, and the political and economic pressures of customers' reactions encourage efforts to enhance efficiencies and reduce costs. The mere existence of comparable municipal utilities operates as a check on the necessarily imperfect regulatory systems that attempt to ensure that consumers receive the highest quality of service at the lowest possible cost. Contrary to the suggestion of *Concord*, therefore, competition is not inconsistent with the regulatory infrastructure of this industry, but in fact facilitates effective regulation.

Where a neighboring franchisee controls its competitor's supply of wholesale power, it can virtually dictate the performance of the municipal system by manipulating its wholesale price of power. Further, it can evade the regulatory and competitive checks provided by yardstick competition and erode customer confidence in the municipal system. This is precisely what happened to the Cities during the period 1976–1979.

The second and third reasons advanced by the *Concord* opinion for refusing to address a price squeeze in a regulated industry are

equally inconsistent with this Court's decisions and with antitrust policy, as well as being self-contradictory. The second reason suggests that if the prices set by regulators accurately reflect costs, only inefficient distributors will be harmed by a price squeeze. *Concord* at 19a. The third reason, however, argues that a prohibition against price squeeze will encourage utilities to set retail prices too high. *Id.* at 20a. Thus, the second reason assumes, contrary to the *Conway* decision, 426 U.S. 271, that regulation is able to determine costs perfectly and precisely, while the third reason assumes that regulation will not be effective in constraining retail rates. More importantly, *both* the second and third reasons presume that retail competition has no value in encouraging efficiency or restraining prices.

The fourth and fifth reasons argued in support of the *Concord* "abstention" doctrine invoke considerations of administrative difficulty, regulatory flexibility, and judicial economy. Again, these arguments are fundamentally incompatible with antitrust policy. While it is true that price squeeze claims raise difficult issues, that is no less true with respect to many (or most) antitrust claims, as well as other complex litigation.[8] With respect to the potential for interference with regulatory policy, the *Otter Tail* decision, 410 U.S. 366, balanced the interest in antitrust enforcement against the possibility of conflicts with regulatory policy and concluded that a theoretical conflict should not be permitted to interfere with the application of the antitrust laws. Rather, actual conflicts between regulatory imperatives and antitrust policy should be resolved on a case by case basis. *Otter Tail,* 410 U.S. at 376-77.

Finally, the *Concord* court's contention that there is an adequate administrative remedy for price squeeze is inexcusably myopic for all of the reasons set forth in *Mishawaka I,* 560 F.2d at 1324-25, and at pages 15-17 of the Towns' Petition. Under *Conway,* 426 U.S. 271, the FERC is obliged to consider the effects on competition of the relationship between a utility's proposed wholesale rates and its retail rates. But the remedy available from

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[8] For example, predatory pricing and price discrimination claims also involve inquiries into the relationship between prices and costs.

the FERC is limited to refund of the amount of the price squeeze, plus interest, many years after the fact.[9] The FERC cannot remedy other types of antitrust injury, such as the ones described by the Seventh Circuit in *Mishawaka II*, 616 F.2d at 989. Moreover, even if the FERC were to act promptly to reduce a proposed wholesale rate to diminish or even eliminate a price squeeze, it cannot enjoin the filing of a new discriminatory wholesale rate proposal. Thus, without the deterrent effect of potential liability for treble damages and attorneys' fees and costs or the possibility of injunctive relief under the antitrust laws, utilities could impose one price squeeze after another with total impunity. It is a "no lose" proposition for the monopolist-supplier and a "no win" situation for the victimized wholesale customer-competitor.

To permit, indeed to encourage, deliberate anticompetitive conduct of a monopolist seems unthinkable. *Concord* cannot be harmonized with the fundamental principles of antitrust policy, with the decisions of this Court, or with *Mishawaka II*, *Groton*, or *Kirkwood*. These conflicts should be resolved by granting certiorari to examine the wisdom and propriety of the *Concord* decision.

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[9] For example, almost fifteen years after this Court's decision in *Conway*, the Cities in 1990 finally received FERC-ordered refunds for a price squeeze that occurred in 1976. *See, Southern California Edison Co.*, Opinion No. 284, 40 F.E.R.C. ¶ 61,371 (1987), *on rehearing*, Opinion No. 284-A, 50 F.E.R.C. ¶ 61,275 (1990), *appeals docketed*, No. 90-1236 (D.C. Cir. May 4, 1990), No. 90-1369 (D.C. Cir. July 16, 1990). Both the Cities and SCE have petitioned for review of Opinion Nos. 284 and 284-A. The Cities maintain on appeal that the FERC seriously understated both the magnitude and the duration of the price squeeze, while SCE argues that no price squeeze relief was justified.

II.

CONCLUSION

For the reasons set forth herein, we urge the Court to grant the Petition for Writ of Certiorari.

Respectfully submitted,

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